IFRS

STAFF PAPER

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IFRS Interpretations Committee Meeting

Project	**IFRS 11 *Joint Arrangements***		
Paper topic	Remeasurement of previously held interests—Loss of control		
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Introduction

1. The IFRS Interpretations Committee ('the Interpretations Committee') discussed whether the retained interest in the assets and liabilities of a joint operation should be remeasured when an entity loses control of an asset or group of assets. The asset or group of assets may or may not constitute a business. In the transaction discussed, the entity either retains joint control of a joint operation or is a party to a joint operation (with rights to assets and obligations for liabilities) after the transaction. For ease of reference, this transaction is hereafter referred to as 'loss of control transaction'.

2. Some members of the Interpretations Committee expressed a preference for remeasurement of the retained interest in transactions in which the asset, or group of assets, constitutes a business (as defined by IFRS 3 *Business Combinations*). However, the Interpretations Committee also noted that the loss of control transaction is similar to the accounting for the sale or contribution of assets to an associate or a joint venture, which has been the subject of recent discussions by the International Accounting Standards Board (the 'Board').

3. The Interpretations Committee noted that the Board had amended IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* to address the accounting for the sale or contribution of assets to an associate or a joint venture. Subsequently, the Interpretations Committee and the

Board considered a number of other issues with respect to the sale or contribution of assets between an investor and its associate or joint venture. The Board decided that these issues should be addressed as part of its research project on equity accounting, and deferred the effective date of the amendments to IFRS 10 and IAS 28.

4. Consequently, the Interpretations Committee decided to consult the Board to assess whether it should postpone further discussion of the loss of control transaction until the Board further considers the accounting for the sale or contribution of assets to an associate or a joint venture.

5. We consulted the Board at its meeting in October 2015 to obtain its views.

6. Appendix B to this paper includes additional background information and a summary of the previous analysis and discussions of the Interpretations Committee on the loss of control transaction.

Purpose of this paper

7. The purpose of this paper is to:
   - (a) provide the Interpretations Committee with a summary of the feedback received from Board members; and
   - (b) ask the Interpretations Committee if it agrees with the staff recommendation to postpone further discussions of the loss of control transaction.

Feedback received from Board members

8. At the October 2015 Board meeting, we received feedback from three Board members on the loss of control transaction.

9. One member thought that the Interpretations Committee should wait and see how things evolve regarding the accounting for the sale or contribution of assets to an associate or a joint venture. That member noted that he was not aware of many

loss of control transactions. The member did not think that there was an urgent need for clarity with respect to this transaction.

10. Another member was of the view that it would not be wise to ask the Interpretations Committee to consider the loss of control transaction further at this stage given the difficulties the Board had encountered with the amendments to address the sale or contribution of assets to an associate or a joint venture.

11. The third member thought that, if the Interpretations Committee had reached a conclusion that crossing the control barrier should trigger remeasurement, that member would not be opposed to the Interpretations Committee proceeding to develop a solution on that basis. That member observed that the Interpretations Committee's consideration of the definition of a 'group' in IFRS 10 was helpful in supporting this conclusion.

12. Nonetheless, that member did not wish to ask the Interpretations Committee to consider the loss of control transaction further at this stage if the Interpretations Committee thought that there was a strong link between this transaction and the transactions considered as part of the recent discussions on accounting for the sale or contribution of assets to an associate or a joint venture.

Staff analysis

13. On the basis of the feedback received, we recommend that the Board should consider the accounting for the loss of control transaction at the same time as it further considers the accounting for the sale or contribution of assets to an associate or a joint venture. We do not think the Interpretations Committee should add this issue to its agenda. This is because:

    (a) the conflict that exists between the requirements in IFRS 10 and IFRS 11 *Joint Arrangements* with respect to the loss of control transaction is similar to the conflict that exists between IFRS 10 and IAS 28. In September 2014, the Board issued amendments to IFRS 10 and IAS 28 to address the conflict between those Standards. After issuing those amendments, the Board considered a number of other related issues. The Board decided that these issues should be addressed as part of its research project on equity accounting and also decided to defer the effective date of the amendments to IFRS 10 and IAS 28;

(b) if the conflict between IFRS 10 and IFRS 11 were to be addressed, it would require amendments to existing IFRS Standards. We think it would be more efficient to consider the accounting for the loss of control transaction at the same time as further considering the accounting for the sale or contribution of assets to an associate or a joint venture. This is because of the similarity between the transactions being considered;

(c) any decision reached by the Interpretations Committee with respect to a loss of control transaction may need to be revisited within a short time period if the Board reaches a different conclusion regarding the accounting for the sale or contribution of assets to an associate or a joint venture;

(d) although we acknowledge, on the basis of our outreach, that this transaction is widespread and could result in diversity in practice, we do not think that the need for clarity on this transaction is more urgent than the need for clarity on accounting for the sale or contribution of assets to an associate or a joint venture. On the basis of prior experience, we would expect that loss of control transactions are less widespread than the sale or contribution of assets to an associate or a joint venture; and

(e) none of the Board members who expressed a view noted a strong preference for the Interpretations Committee to develop a solution before a decision is made on the amendments to address the sale or contribution of assets to an associate or a joint venture.

Staff recommendation

14. On the basis of our analysis, we recommend that the Interpretations Committee should not take this issue onto its agenda. We think that the Interpretations Committee should ask the Board to consider the loss of control transaction at the

same time as it further considers accounting for the sale or contribution of assets to an associate or a joint venture.

15. We have set out the proposed wording for a tentative agenda decision in **Appendix A** to this paper.

Questions for the Interpretations Committee
1. Does the Interpretations Committee agree with the staff recommendation not to add this issue to its agenda? 2. Does the Interpretations Committee have any comments on the proposed wording of the tentative agenda decision set out in Appendix A to this paper?

Appendix A
Proposed wording of the tentative agenda decision

IFRS 11 *Joint Arrangements* and IFRS 10 *Consolidated Financial Statements*—Accounting for loss of control transactions

The IFRS Interpretations Committee ('the Interpretations Committee') discussed whether an entity should remeasure its retained interest in the assets and liabilities of a joint operation when the entity loses control of an asset or group of assets. In the transaction discussed, the entity either retains joint control of a joint operation or is a party to a joint operation (with rights to assets and obligations for liabilities) after the transaction. The asset, or group of assets, over which the entity loses control may or may not constitute a business.

The Interpretations Committee noted that paragraphs B34–B35 of IFRS 11 *Joint Arrangements* specify that an entity recognises gains or losses on the sale or contribution of assets to a joint operation only to the extent of the other parties' interests in the joint operation. The requirements in these paragraphs could be viewed as conflicting with the requirements in IFRS 10 *Consolidated Financial Statements*, which specify that an entity should remeasure any retained interest when it loses control of a subsidiary.

The Interpretations Committee observed that the International Accounting Standards Board (the 'Board') had issued amendments to IFRS 10 and IAS 28 *Investments in Associates and Joint Ventures* in September 2014 to address the accounting for the sale or contribution of assets to an associate or a joint venture. Those amendments address a similar conflict that exists between the requirements in IFRS 10 and IAS 28. After issuing the amendments, the Board considered a number of other related issues. The Board decided to address these issues as part of its research project on equity accounting, and also decided to defer the effective date of the amendments to IFRS 10 and IAS 28.

Because of the similarity between the transaction being considered by the Interpretations Committee and the accounting for the sale or contribution of assets to an associate or a joint venture, the Interpretations Committee concluded that the two transactions should be considered concurrently by the Board. Consequently, the Interpretations Committee [decided] not to add this issue to its agenda but, instead, to recommend to the Board that the issue is considered at the same time that the Board further considers the accounting for the sale or contribution of assets to an associate or a joint venture.

Appendix B: Background and summary of previous analysis and discussions

B1. The following section sets out additional background information and provides a summary of the staff analysis and previous discussions of the Interpretations Committee on the loss of control transaction.

Background

B2. An entity may enter into a transaction as a result of which it loses control of a business. The transaction results in the entity having joint control of, or being a party to, a joint operation after the transaction. The question is: how should the entity account for its retained interest after this transaction.

B3. Our outreach indicated that in situations in which the asset, or group of assets, meets the definition of a business, the transaction is widespread. We understand that there are three differing views that have developed in practice:

(a) *View 1—the entity remeasures its retained interest at fair value*

Proponents of this view note that paragraph 25 of IFRS 10 contains requirements regarding a loss of control transaction and requires an entity to remeasure retained interests.

They also note that paragraph BCZ182 of IFRS 10 states that, in the Board's view, the loss of control is a significant economic event, which results in a change in the nature of the investment. This same rationale is also applicable to the loss of control transaction.

(b) *View 2—the entity does not remeasure its retained interest*

Proponents of this view think that paragraph 25 of IFRS 10 is intended to address only the scenario in which an entity subsequently accounts for the retained interest as a financial asset or as an investment in an associate or a joint venture. Those requirements are not applicable to a loss of control transaction that results in the entity having joint control of, or being a party to, a joint operation after the transaction. They think that an entity should not derecognise or remeasure the share of assets and liabilities of the joint operation in which it retains an interest.

They also note that paragraphs B34–B35 of IFRS 11 contain specific requirements on accounting for the sale or contribution of assets to a joint operation. The requirements specify that an entity recognises gains or losses only to the extent of the other parties' interests in the joint operation.

(c) *View 3—the entity remeasures its retained interest only if the joint operation is structured through a separate legal entity.*

Proponents of this view note that the requirements in paragraph 25 of IFRS 10 apply only to the loss of control of a subsidiary. Appendix A of IFRS 10 defines a subsidiary as an entity that is controlled by another entity. Accordingly, proponents of this view distinguish the accounting for the loss of control depending on whether the business is 'housed' in a separate legal entity. Applying view 3, if a business is housed in a separate legal entity, an entity would apply the requirements in paragraph 25 of IFRS 10 and would remeasure any retained interests.

Summary of the staff analysis and the Interpretations Committee's discussions

B4. The Interpretations Committee discussed the accounting for retained interests in a loss of control transaction at its meeting in September 2015 (click here to access a copy of the agenda paper and click here to access a copy of the *IFRIC Update* from the meeting in September 2015).

B5. The Interpretations Committee noted that the key factors to use in assessing whether an entity should remeasure retained interests are:

(a) the significance of the underlying economic event; and

(b) the measurement model applicable to the recognition of the retained interests.

B6. For transactions involving a business, our analysis noted that:

(a) *the transaction represents a significant economic event.*

This is because the entity has surrendered its controlling interests in exchange for being either a passive investor (ie a party to the joint operation) or a joint controller in the joint operation. In effect, it has surrendered its right to unilaterally *direct* how the acquiree and its management use those assets in its operation. It no longer has *unilateral decision-making power* over the relevant activities of the business. We think that the loss of control transaction changes the nature of the investment and the relationship between the parties.

(b) *the fair value model set out in IFRS 10 in relation to the loss of control is the appropriate measurement model to apply to this transaction.*

IFRS 11 requires a joint operator to account for the assets, liabilities, revenues and expenses relating to its interests in a joint operation in accordance with applicable Standards. Some of those Standards, such as IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*, provide a cost-based model for initial recognition.

IFRS 10 requires an entity to remeasure its retained interest at fair value when it loses control of a subsidiary. IAS 28 *Investments in Associates and Joint Ventures* uses a cost-based model, because it specifies that an investment in an associate or a joint venture is recognised at cost on initial recognition (see paragraph 10 of IAS 28). However, paragraph 25(b) of IFRS 10 notes that an entity should regard the remeasured value of the retained interest to be its cost on initial recognition of an investment in an associate or a joint venture.

Consequently, we think that the fair value model set out in IFRS 10 in relation to the loss of control of a subsidiary is the appropriate measurement model to apply to this transaction.

B7. Our conclusion was that an entity should remeasure its retained interest after the loss of control transaction. We also did not think that the structure of the joint operation (ie whether there is a legal entity in place) should result in a different accounting outcome.

B8. At the Interpretations Committee meeting in September 2015, a number of members agreed with our analysis and expressed a preference for remeasurement of the retained interests in transactions in which the asset, or group of assets, constitutes a business.

B9. A few members also noted that they have had some experience with loss of control transactions not involving a business and suggested addressing transactions involving a business, and those not involving a business, together.

B10. However, there have been recent Board discussions on a related transaction: the sale or contribution of assets to an associate or a joint venture. Consequently, our analysis noted that the outcome of those discussions could have a direct effect on the Interpretations Committee's analysis. Details of the interrelationship are discussed below.

Similarity to an amendment made by the Board

B11. In instances in which an entity retains an interest in the former subsidiary that results in that subsidiary becoming an associate or a joint venture, the Board noted a conflict between the requirement to eliminate gains or losses resulting from downstream transactions with an associate or a joint venture in IAS 28 compared with the requirement to recognise, in full, gains or losses resulting from the loss of control of a subsidiary.

B12. In order to address this conflict, the Board made some amendments to IFRS 10 and IAS 28 in September 2014. The Board decided that when the asset, or group of assets, contributed to an associate or a joint venture meets the definition of a business, an entity is required to recognise full gains or losses and remeasure this retained interest at fair value. When the asset, or group of assets, contributed to an associate or a joint venture does not meet the definition of a business, an entity recognises only partial gains or losses (to the extent of the unrelated investors' interests).

B13. The amendment to IFRS 10 specified that when an entity retains an interest in a former subsidiary that results in an investment in either an associate or a joint venture that is not a business, an entity remeasures its retained interest at fair value. However, the entity should eliminate the part of the gain or loss associated with the entity's retained interest in the associate or joint venture against the carrying amount of the retained interest. In situations in which the retained interest is a financial asset, an entity measures the retained interest at fair value and recognises the gain or loss resulting from the remeasurement in profit or loss.

B14. This results in an entity's measurement of its retained interest after the transaction being dependent on whether the transaction involves a business and the nature of the retained interest (ie whether it is a financial asset or an investment accounted for using the equity method).

B15. After issuing this amendment, the Board considered proposing a further narrow-scope amendment to clarify some matters linked to the amendment. However, the Board decided that those issues should instead be addressed as part of the research project on the equity method of accounting. Accordingly, the Board has decided to defer the effective date of these amendments, in order to avoid making multiple changes to the Standard within a short period of time.

B16. A similar conflict exists for joint operations. Paragraphs B34–B35 of IFRS 11 specify that an entity recognises gains or losses on the sale or contribution of assets to a joint operation only to the extent of the other parties' interests in the joint operation. The requirements in these paragraphs could be viewed as conflicting with the requirements in IFRS 10 to remeasure any retained interest when an entity loses control of a subsidiary.

B17. The Interpretations Committee noted that it may be able to reach a consensus on the appropriate accounting treatment for the loss of control transaction (for example, a number of members expressed a preference for remeasurement in cases in which the transaction involved a business). The Interpretations Committee asked us to consult the Board to assess whether it should continue its deliberations or instead postpone further discussion.